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HARMONIZATION AND RECOGNITION OF PROFESSIONAL QUALIFICATIONS

Background note by the UNCTAD secretariat

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Introduction

1. The UNCTAD secretariat prepared this note pursuant to paragraph 3 (i) of the work programme of the Standing Committee on Developing Services Sectors (TD/B/39(2)/2) whereby it was decided to analyse on-going processes of recognition and harmonization of qualifications.

2. The multilateral effort to liberalize trade in services in the Uruguay Round identified differing qualification systems and standards in professional services among countries as constituting barriers to trade in these services. In the context of regional and bilateral trade negotiations on services, processes of recognition and harmonization are underway, but such experiences indicate that these processes are complex and are hampered by the multiplicity of standard-setting and enforcement bodies, as well as by general lack of information.

3. In initiating work under paragraph 3(i) of the work programme, this note contains background information on harmonization and recognition of qualifications. It reviews laws and regulations in the professional service sector, highlighting those which are inherent to qualifications and standards, as well as initiatives taken at the government and private sector levels to achieve harmonization and recognition of qualifications. It also identifies areas where further work could be conducted by the Standing Committee in order to promote the mutual recognition and harmonization of qualifications among countries.

I. Internationalization of professional services

4. This document focuses on accredited professional services, as ongoing efforts to achieve recognition and harmonization of qualifications are addressed to these services. Activities generally considered to be accredited professional services include: legal professions, legal advice/consultancy, accountancy services, architectural services, construction and engineering services, quantity surveying, health services, linguistic services, others (e.g. estate agents, patent agents, etc).[1] The Western liberal professions have been serving clients around the world for a long time. Engineers have sold their services in foreign markets for up to two centuries, and in 1986 European firms held a 55 per cent share of the international engineering design market.[2] Other professions, such as accountants, lawyers and architects, have exported their services for over 80 years. Responding to client demand, accountants have built up networks of partnerships (organised in many different ways) covering virtually the whole world.

5. There are different degrees of market concentration among the services in this category, ranging from large TNCs to a multitude of small firms. Accountancy firms with headquarters in the United States sell their services in foreign markets largely from their 3,570 foreign affiliates, which are almost three times as numerous as their European-based counterparts. Of the 40 firms represented in a sample in Europe, 27 were United States-owned, 10 were EC-owned, and 3 were owned by Japan. Lawyers have become concentrated in various centres (New York, London, Paris, Hong Kong, Tokyo and so on), but their networks do not match in size or scope those of the accountants; surveyors are also in this category. Some engineering consultants operating internationally are large, but probably none approach the size or turnover of the large accountants or management consultants. Architects work mainly in small firms, as do patent agents.

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[1] See Chapter VI: Services, in " UNCTAD VIII, Analytical report by the UNCTAD secretariat to the Conference", TD/358, January 1992.

[2] Y. Soubra, "The construction and engineering design services sector", *Journal of World Trade*, Vol. 23, No. 1 (1989).

6. International trade in professional services involves cross-border trade, commercial presence, and the international movement of persons. Even though independent practitioners are becoming increasingly common, international trade in the sector is done primarily by firms through some form of commercial presence. In order to supply services successfully, firms have to be well entrenched in the local market and perceived to be conversant with national customs and mores to an extent comparable to indigenous firms. Some transnational firms are networks of national firms which have benefited from foreign investment, including crucially the training of local personnel in standards of service quality and management know-how, as well as from spending on equipment and communications facilities. A small survey of member firms, including some professional and business services suppliers, carried out in 1989 by the United States Coalition of Service Industries showed that their subsidiaries in developing countries, which employed nearly 44,600 people, had recruited 99 per cent of their staff locally. The equivalent figure for the top 842 senior management positions was over 83 per cent. The networking used by firms in the modern professional services sector creates a two-tier market, i.e. a few large firms, supported by their access to intra- and intercorporate information networks, supplying multinationals and large local firms, with more numerous small firms supplying small and medium-sized domestic enterprises.[3]

7. Over the past two decades, improvements in telecommunications and computing, as well as falling transport costs, have fuelled the development of global manufacturing processes, distribution networks and marketing plans. The trend to a higher information content in goods has prompted TNCs to plan and control their operations on a global scale, whilst producing many product variations to match local tastes and needs. Large increases internationally of intra-industry and intra-firm trade flows for goods have obliged the suppliers of professional services to manufacturers to match their organizations, service standards and locations to the new global/local patterns of their clients. Similar patterns can be seen in the way service firms, especially in financial services, transport and telecommunications sectors, have responded to the demands of service TNCs.

8. Although the suppliers of professional services have been greatly affected organizationally by this demand trend, the impact of information technology on the complex nature of their client relationships has been less dramatic. Whilst communications have improved their ability to transfer, combine and select information, and have made various backroom processes more efficient and cost effective (e.g. invoicing, accounting, detailed design calculations, information retrieval and so on), the need for more highly qualified and well paid staff has increased, and most of these are involved in direct inter-personal relations with clients at the latters' locations. For this reason employment growth of intermediate professional and business services has been greatest where the TNCs are located, and TNC suppliers have invested in wide networks of local firms, staffed by local personnel who have been trained up to international standards of competence, service and management know-how and in the use of modern equipment.[4]

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[3] Thierry Noyelle, "Business services and the Uruguay Round Negotiations on Trade in Services", *Trade in Services: Sectoral Issues* (UNCTAD/ITP/26), pp. 309-63; Sieh Lee Mei Ling, "Professional Business Services in ASEAN and the Uruguay Round Trade Negotiations", *Services in Asia and Pacific: Selected Papers*, Volume One (UNCTAD/ITP/51), pp. 35-74.

[4] A. Leyshon, P. W. Daniels and N. J. Thrift, "Internationalization of Professional Producer Services: The Case of Large Accountancy Firms", Working Papers on Producer Services No. 3, Service Industries Research Centre (SIRC), Portsmouth, United Kingdom, 1987.

II. Regulations affecting trade in professional services

9. The notion of the independent professional adviser first surfaced in nineteenth century Britain, and an early twentieth century definition stated that "a profession is a vocation founded upon specialized educational training, the purpose of which is to supply disinterested counsel and service to others, for a direct and definite compensation, wholly apart from expectation of other business gain".[5] At the heart of the concept lie the ideals of vocation, disinterested counsel and service, which demand a relationship of trust between equal humans, and not one of master and servant as in contracts of employment. This early development was predicated on assuring standards of competence, ethical behaviour and personal accountability of an identifiable individual of integrity, who was independent of other pressures, whether religious, political or financial. The focus then was more on private individual consumers, who in many cases cannot assess the nature or standard of the service, or its results (unless too late), which can deeply affect their health, safety, and assets of both them individually and often those of a broader public (termed the supra-client responsibility of the professional). The purpose of qualifications and codes of conduct, with all they imply, was to give assurance, and hopefully prevent such misfortunes as a consumer undergoing the wrong surgical operation, receiving faulty legal advice, living in a structurally unsound house, or losing his assets.

10. Although conditions vary widely between different countries in the level of state regulation and self-regulation, if professional services suppliers are put into categories according to the degree of regulation, they could be grouped as follows: highly regulated - accountants/auditors/tax advisers, medical doctors, lawyers, insolvency practitioners; and less regulated - architects, engineers, surveyors, patent agents, real estate agents, placement/recruitment. Diplomas evidencing standards of competence are prevalent in these services. If it were postulated that some types of knowledge are of universal application (e.g. the sciences of chemistry and physics) whilst other knowledge is local (e.g. Japanese law), then this might be a factor in the rationale for strict regulation. Management know-how is required by all producers and is of a universal nature, but apart from this, these professions might fall into the following three categories, according to the application of their core knowledge: mainly universal - accounting, engineering, healthcare; mixed - architects, surveyors; mainly local - auditing and taxation advice, legal, real estate agents, placement and recruitment. Where the core knowledge is characterized as mainly local, it is possible for it to be supplied by locally licensed TNC affiliates, except in the case of the most highly regulated or restricted activities, for example audit and tax returns, and legal transactions, especially to do with land and other property, where local notaries often have a monopoly in certain procedures.

11. In general, regulations deal with the competence of individual practitioners, their practice activities, and their adherence to professional codes of conduct. Competence is gained from education and practical training, and is evidenced by diplomas awarded on the results of examinations. Behaviour in practice cannot be assured in advance, and has to be conditioned by ethical codes and enforced by disciplinary procedures. Government regulations can include restrictions on practice activities, and even the prohibition of some; in certain cases this can result in the denial of access to professionals who have the necessary qualifications for reasons not based on grounds of competence. Most regulations are laid down by Governments, whether at a federal or State level, but in some countries, the responsibility for examining competence and laying down rules of conduct lies with private bodies in the educational and professional fields. These bodies may or may not be specifically mandated for these responsibilities by Governments.

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[5] Sidney and Beatrice Webb, *New Statesman*, 2 April 1917.

12. Although auditing firms are normally required to be locally owned in order to prevent mergers and acquisitions across borders, they prefer to be associated with internationally reputed auditing firms. This is because for accounting services, particularly for auditing large firms and for providing financial consultancy to them, internationally established names are crucial for obtaining clients. The names are regarded as assurance for reliable services, supported by the ability to supply services to various markets locally by high-quality staff connected with international networks of accountants through modern telecommunications and information facilities. In the area of legal services as well, similar regulations on local control of firms exist in many countries. However, legal firms who service large clients tend to favour international association for similar reasons as in auditing. Such regulations may render difficult the exapansion of relatively large professional service firms.

13. The export of professional services depends on the freedom to move people, information and money across borders, to retain freedom of choice over the form of establishment, including the nature of its legal entity, the choice of local professional or business partner and the form of association with him, the use of an international firm name, and the freedom to carry out the practice activities in question. Regulations covering the movement of people raise issues of immigration and the public or general good, or are aimed at the protection of the consumer, and relate to competence and practice control, activities, and conduct. Here regulatory systems for the liberal professions do not distinguish between business purchasers and individual consumers: the level of protection afforded to both is the same, unlike in the financial services field within the EC, where wholesale supply to producer firms is less restricted. Concerns over the movement of information tend to be related to copyright protection for information abstracted from databases and for proprietary manuals incorporating critical know-how (akin to computer software), privacy laws (relating to sensitive information on individuals), and the location of data processing. In the main, information flows remarkably freely, by the mode of choice, and processing can be carried out wherever desired. There are some countries with laws which may be lax on the protection of copyright and proprietary know-how, or restrictive on data privacy and processing.

14. The barriers to trade in professional services identified include: non-accreditation, non-recognition of foreign qualifications, denial of access to examinations for completion of qualifications, non-recognition of non-citizens or non-residents requirement of joint venture or prohibition of joint venture, local establishment requirements, foreign exchange controls affecting the repatriation of earnings by firms, restriction of staff that could be employed, mandatory use of local consultants, discriminatory regulation of fees and expenses, discriminatory purchasing arrangements, entry restrictions such as visa restrictions, prohibition of using firm's name, denial of access to transborder data flows or telecommunication services, the use of subsidies or other forms of official support being granted to domestic suppliers, and anti-competitive practices of TNCs.[6]

15. Trade in professional services can take place through all modes of delivery. However, as information on the forms of such trade is limited, it is difficult to assess to what extent each barrier affects trade in professional services. For example, the export of accounting and legal services requires some sort of establishment and the movement of a few key personnel. However, most of the work involved is undertaken by local personnel, the movement of support staff or through transborder data flows. For construction services, the movement of a few key personnel and a relatively large number of support staff is necessary. Although medical doctors and other healthcare professionals almost invariably deal with the individual final consumers, their services can be purchased by firms to run internal clinics and screening for employees -

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[6] Philippe Brusick, Murray Gibbs and Mina Mashayekhi, "Anti-competitive practices in the services sector", *Uruguay Round: Further Papers on Selected Issues*, UNCTAD/ITP/42), pp. 129-51.

especially in difficult overseas locations with inadequate or non-existent local medical facilities. In the case of exports of medical services (e.g. nursing), the movement of accredited personnel is a major mode of supply, although it can be conducted through the movement of consumers. Professional medical services also form a crucial part of the operation of commercial hospitals and clinics set up overseas, or operated for state authorities. To this extent there is an export of medical services through commercial presence, combined with some movement of persons as suppliers and much more as consumers.[7] Further work in this area might address the forms of trade in professional services in order to assess more precisely how these barriers affect trade in different professional services.

16. The regulation of the liberal professions in federal countries is mostly at the provincial or state level, except in regimes of Hispanic origin. Since national treatment normally prevails (in the EC this is termed Host Country Control), internationally the key matters are competence and practice control, activities and conduct, and the latter are seldom, if ever, covered by intergovernmental agreements.

17. Apart from the current conditional offers on the movement of natural persons to be included in the Schedule of Commitments annexed to the Uruguay Round General Agreements on Trade in Services (GATS), there are no multilateral agreements which deal with the movement of people. However, commitments on such movement have been included in customs unions, free trade agreements[8] or other bilateral or subregional arrangements. As to the other modes of delivery mentioned, regulations relating to the testing of competence or the disciplining of professional conduct can be relevant. There are other matters of importance such as avoiding double taxation, gaining access to local banks and credit facilities, and buying or leasing land or buildings, but these are usually distinct from competence and behaviour issues.

III. Licensing

18. Historically, private societies in the professions were first formed with the aim of giving assurance to the public and this involved setting educational standards, awarding diplomas, qualifications and titles, and operating disciplinary procedures. Many of these societies applied to the Government for official recognition of their status and licensing activities by means of a charter or similar mandate. Such societies continued to be formed as new specialties developed. This pattern spread from the United Kingdom, especially to the Commonwealth countries, but also to many others, such as the United States, where the intrinsic merits of such group standards were appreciated. Certain activities were often reserved for those with particular qualifications and titles, and an official charter enabled such monopolies to be enforced. In some cases, now mostly banned under competition laws, minimum fee scales were also backed by law. In many countries around the world, there are restrictions imposed by the state as to who, for example, may represent a client in a court of law, draw up and authenticate contract documents, audit the books of account of companies, apply for building approvals, undertake surgical operations, and so on. Gradually, in many countries the state has taken the responsibility for the major liberal professions, consigning many professional groups to the status of private societies with optional membership and with no licensing authority. The state also employs significant numbers of professionals, making their employment subject to the holding of the right qualifications. Most regulations

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[7] Trade in medical services involves additional considerations such as the geographical scope of insurance coverage. UNCTAD, in cooperation with the Pan American Health Organization (PAHO), is conducting a pilot study on trade in this sector.

[8] See TD/B/CN.4/24.

are laid down by Governments, whether at the federal or State level, but in some countries, the responsibility for examining competence and laying down rules of conduct lies with private bodies in the educational and professional fields. These bodies may or may not be specifically mandated for these responsibilities by Governments. Any list of official and private sector licensing and professional bodies would be enormously long.

IV. Mutual recognition and harmonization

A. Mutual recognition

19. In many cases, where professional societies in different countries were self-regulating, they negotiated agreements to recognize each others' qualifications. Examples of such agreements can be found in most of the professions. In contrast, where the state is the regulator, recognition necessitates official bilateral agreements, of which there are very few examples. The original purpose of recognition was to provide a route for individuals to continue earning a living in their profession if they moved from one country to another for personal or economic reasons, without the obligation to requalify, which might impose unacceptable losses in terms of time and earnings. In practice, in most professions such movement has not involved more than a very limited number of individuals, though there has been concern in the medical field in some developed countries as to the possibility of immigration in larger numbers, possibly coupled with pressure on the professions to reduce or alter standards. The problem of recognition even exists among provinces and states within countries, complicating further the processes of mutual recognition of qualifications among countries.

20. Negotiations of mutual recognition of qualifications and licenses are often conducted in a bilateral and reciprocal manner by Governments or the competent authorities. The principal factors covered by agreements on mutual recognition include education, training, qualifications, diplomas, the uses of titles, and behavioral and institutional matters such as fitness, ethical codes, discipline and co-operation between the competent authorities. Of necessity, such agreements begin at the bilateral level. In some federal jurisdictions it has been possible for authorities to co-operate so that the final outcome has been a plurilateral agreement for recognition, such as those between certain states in the United States and between the Commonwealth, state and territorial governments in Australia. In the EC, some progress has been made with respect to mutual recognition among member States of the competence of individuals, but the first three years of university level education, not at the professional level. One major exception is the case of the healthcare professions and architects, where harmonization directives have achieved mutual recognition at the level of full professional qualifications. This is not the case with other principal suppliers of professional business services, namely accountants and lawyers. In the case of audit practice, cross-border trade in general is not permitted, and the question of mutual recognition does not, therefore, arise.

21. Without a recognition agreement being in place between two countries, a foreign citizen would only be allowed to practise following a full revalidation procedure to ensure his competence. This could involve attendance at local courses at specified educational institutions, both academic and professional, for the appropriate number of years, including supervised practice periods, and followed by examinations and registration procedures. Where mutual recognition agreements are attempted, it is usual to assess the body of knowledge, examinations, codes and enforcement procedures, and agree on either shorter revalidation education, and with the usual examinations, or alternatively to test for material differences in the body of knowledge (usually relating to local conditions, laws, administrative procedures, standards, customs, and so on), leaving practitioners free to acquire the additional knowledge in their own way. After these tests, professionals would be permitted or required to register

locally so as to ensure adherence to the local code and mandated activities, if any.

22. Apart from partnerships, where there is no legal persona separate from the individual partners, firms have a separate juridical persona, and they can be given some supervisory responsibilities by authorities. Ensuring the qualifications and codes of conduct of people who own, control, manage and practise from the subsidiaries and branches of firms which are not under local control may sometimes present difficulties, as control and management could be exercised from abroad by people whose qualifications may be difficult to ensure. In the EC, for example, even though firms have the right to establish or open branches, in the professional field their activities are controlled by the host country, as there is no mutual recognition of licenses for firms to practise.

B. Harmonization

23. While recognition is based on the concept of accepting others' qualifications, harmonization involves a more complex process of establishing unified qualification systems and standards. Harmonization of qualifications and standards, like that of technical standards for physical products, is often facilitated through multilateral procedures. The experience of the European Community referred to in a later section of this document suggests that mutual recognition, together with some form of supplementary device to fill gaps in requirements, is a preferred approach to harmonization, and it is often an initial step towards the harmonization of qualification systems and technical standard requirements.

24. In 1986, at their annual conference, the Coalitions of Service Industries discussed the recognition and harmonization of professional standards. They warned that the application of national treatment alone could come into conflict with the recognition of professional qualifications, because whilst national treatment is a necessary condition, it is not a sufficient one. They emphasized that an additional system would be needed to achieve equivalent treatment, based on the principle of home country control, whereby there is accepted documentary proof available that the holder has been awarded a specific qualification. This system could only be implemented by detailed bilateral negotiations. The alternative, a general system of harmonization for the mutual recognition of degrees, diplomas, and qualifications, would be a much longer and difficult process. The way ahead would lie in the mutual recognition of national standards bilaterally agreed upon.

V. Private sector mutual recognition agreements

25. There are many examples of institutes in different countries agreeing on recognition of each other's certificates without the involvement of their respective Governments. There is no active global inter-professional group to match cross-sectoral organizations equivalent to those that exist at national and regional levels, e.g. the UK International Professional Group in London and SEPLIS in Brussels.

26. Box 1 provides some examples of international private bodies involved in issues concerning the recognition of professional qualifications. Those most active in pursuing international mutual recognition arrangements are the accountants, who have prepared carefully co-ordinated proposals on mutual recognition of qualifications and benchmark standards, supported by leading national institutes and their regional organizations. Lawyers are active on mutual recognition of ethical standards at the national level and in Europe at the regional level, but there is no single forum for this at the international level on this subject. There is no co-ordination internationally between the major professions in construction and engineering design. The International Federation of Consulting Engineers is promoting a model code of ethics for member organizations, but is not working on mutual recognition of qualifications, nor

Box 1
International private bodies in professional services: some examples

Accountancy:

International Federation of Accountants (IFAC), New York and Geneva.
International Accounting Standards Committee (IASC), London.
Federation of European Accountants (FEE), Brussels.

Architects:

International Union of Architects (IUA).
Commonwealth Association of Architects (CAA).
Architects' Council of Europe (ACE), Brussels.

Engineers:

International Federation of Consulting Engineers (FIDIC), Lausanne.
Federation of National Engineering Associations (FEANI), Paris.
European Federation of Engineering Consultancy Organizations (EFCA), Brussels.

Surveyors and Construction Cost Consultants:

International Federation of Surveyors (FIG), Canberra.
European Federation of Valuers of Fixed Assets (TEGOVOFA), London.
Association Européenne des Experts du Bâtiment et de la Construction (AEEBC), London.
European Committee of Construction Economists (ECCE), London.

Legal Services:

International Bar Association (IBA).
Council of the Bars and Law Societies of the European Community (CCBE).
Union of European Practitioners in Industrial Property (UEPIP), Brussels.
International Union of Latin Notaries (UINL), Paris.
Federation of Chartered Patent Agents International (FICPI), London.

Medical services:

Standing Committee of Doctors of the EEC (CPM).
World Congress of Physical Therapy (WCPT), HQ in London.
World Federation of Occupational Therapists (WFOT).
European Association for Psychotherapy, Vienna.

Cross-Sectoral Organizations:

World Union of Professions (UMPL), Paris.
Société Européenne des Professions Libérales (SEPLIS), Brussels.
European International Consultants Association (OICE), Geneva.
Eurochambers, Brussels.

Box 2
Recognition agreements in the private sector: examples

The Commonwealth Architects Association

In 1987 the Commonwealth Architects Association had recognition agreements between 31 institutes in the Commonwealth countries, based on the inspection and accreditation of the architectural training provided in specific educational establishments. Qualifications were mutually accepted subject to local interview. The validation of courses and examinations for exemption are carried out on behalf of member institutes by the Royal Institute of British Architects, using procedures modelled on its own practices which have been developed for almost 100 years. Over the years the RIBA's recognition system has extended beyond the Commonwealth in a process which has accelerated recently.

Former US-UK Inter-Recognition Agreement for Architects (July 1987 version)

This agreement was made between the National Council of Architectural Registration Boards of America (NCARB) and the Architects' Registration Council of the United Kingdom (ARCUK), and superseded an earlier version dating from 1972. It was ended in 1990 when the US withdrew. A similar agreement existed with the Australian Institute, which was also unilaterally terminated by the Americans. Each party agreed to grant its certificate to any registered architect of the other, provided they completed certain procedures. They also agreed that either party could enter into similar agreements with registration authorities of other nations, provided they kept each other informed, but persons from third countries so registered by one party under such further agreements could be denied inter-recognition by the other. NCARB, as a non-governmental, national federation of official state boards of registration, could not ensure that a registered person acquiring a certificate under the procedures in the agreement would be admitted to practise by its member state boards, although it would use its best endeavours. The two parties set up a Joint Committee composed of four members from each, with annually alternating Chairman and Vice-Chairman nominated by the groups respectively. Action required a majority in each group, and the chairman did not hold a second or casting vote. Each party would promptly notify the other of any refusal to register an applicant, together with the grounds for refusal, and of the removal of any registered person from the other party, giving the grounds (except where fees were not paid).

The procedures to admit applicants were as follows: *(i) Qualified architects registered with ARCUK applying to NCARB for certification:* After detailing the administrative procedures (to do with registration, prescribed forms and fees) laid down, the agreement required the applicant to attend an interview and examination, for the purpose of demonstrating "knowledge of the practice of architecture in the US". The areas in which the applicant might be interviewed were: (a) Education and Training; (b) Practice and Professional Relations; (c) Exhibition of Projects; and (d) Professional Administration. Once it was determined that all standards had been met, a certificate would be issued upon receipt of a fee. Thereafter the applicant would complete forms to apply for registration with the appropriate State Board, and be advised of all other requirements to complete the procedure. Although statutes which govern the practice of architecture in each US jurisdiction are mostly not the same, most do accept the NCARB certificate without additional interview or examination. Annual renewal of the NCARB certificate is necessary upon submission of a statement of activities during the current year and payment of a renewal fee. NCARB was able to refuse to interview any person registered with ARCUK under the EC architects' directive (85/384/EEC) procedures. It was noted that NCARB was able to refuse to interview a registered person resident in Canada until US architects were granted reciprocal rights there. *(ii) Qualified architects registered with NCARB:* The procedures and requirements were a mirror image, though simpler because the UK constituted one jurisdiction for these purposes, and ARCUK was the sole authority for registration.

are architects, surveyors and planners. Box 2 presents examples of mutual recognition agreements in the private sector among architects. Some of the medical and healthcare professions have world-level bodies, and some of these are developing common training programmes to underpin mutual recognition of qualification processes.

27. The signs are that, with few exceptions, the professional service sectors are responding, though at varying speeds and with varying degrees of success, to market trends and demands for their services, by organizing at regional and global levels. Their organizations appear to be willing to engage in a dialogue with government authorities at all levels to devise ways of constructive co-operation. This has naturally been best developed at the national level, and is substantial in some regions, especially under the stimulus of the EC single market and various free trade agreements. The dialogue has been much less developed, and is virtually lacking for many sectors, at the international level. However, the entry into force of the Uruguay Round General Agreement on Trade in Services should stimulate this process.

VI. Mutual recognition agreements between Governments

A. Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA)

28. Under ANZCERTA the Australian and New Zealand Governments are preparing for negotiations on a mutual recognition agreement covering goods and persons registered to undertake a trade or profession in either country. They hope to use as a model the mutual recognition agreement internal to Australia, which is soon to come into force (described in Box 3). This relies on the principle of equivalence of occupations when considering activities involved and standards necessary to protect consumers. It should achieve a higher degree of home country control than under any other model, but the host state will still retain final control.

29. The mutual recognition proposal would not affect the operation of laws that regulate the manner in which occupations are carried on in New Zealand, so long as these laws: (a) apply equally to all persons carrying on or seeking to carry on the occupation; and (b) are not based on the attainment or possession of qualifications and or experience relating to fitness to carry on that occupation. In the context of a person registered to practise an occupation in an Australian state, that person would be eligible to carry on an equivalent occupation in New Zealand subject to compliance with those New Zealand occupational regulation requirements unrelated to entry requirements.

30. With respect to the definition of "equivalent occupation", the situation current in Australia might be followed, which would imply that coverage under mutual recognition will effectively be determined by the local registration authorities and the appeal process, since a local registration authority is able to declare that an occupation is not equivalent where it is satisfied that the occupation is not substantially the same, and these decisions may be appealed or overruled by agreement between Ministers that an occupation is equivalent.[9]

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[9] One example concerns the requirement in New Zealand for a registered skin diver to be trained in the operation of a decompression chamber, which is interesting in that it demonstrates how in some occupations (and the medical and para-medical professions are further cases) practical training must be undertaken in the use of equipment, usually under supervision of a qualified person. The mutual recognition proposal would only apply where an occupation was registered in both countries.

Box 3
Mutual Recognition Agreement Internal to Australia

A Mutual Recognition Agreement was signed by the Commonwealth Government and the governments of the states and territories in May 1992, for entry into force in March 1993. The goal is the freedom of movement of goods and services in the Australian national market. The decision to establish the scheme arose out of concerns that states and territories were applying different mandatory standards for goods and registration requirements for occupations. With some exceptions it was decided to follow the mutual recognition route, as it was accepted that different mandatory standards and registration requirements could still provide adequate protection for health, safety and the environment.

The mutual recognition model for occupations agreed to by the Commonwealth and state authorities accepts that a person who is registered in one state to practise an occupation, is entitled: (a) to be registered in an equivalent occupation in the other state; and (b) pending such registration, to practise the occupation in the other state. The underlying principle of mutual recognition as it applies to occupations is that persons registered to practise an occupation in one state should be permitted to practise in any other state subject to the occupations being equivalent. The converse of this would be that someone who has been struck off the register in one state would not be able to practise in another.

An occupation for which a person is registered to practise in one state is equivalent to an occupation for which that same person could be registered in another state if the activities carried out are substantially the same. The mutual recognition proposal provides that conditions may be imposed on registration so as to achieve equivalence between occupations in different states.

A local registration authority may refuse to grant registration it if decides that an occupation in which registration is sought is not an equivalent occupation, and equivalence cannot be achieved by the imposition of conditions. Local registration authority decisions may be appealed, and the Australian Administrative Appeals Tribunal could declare occupations carried on in two sates are not equivalent (a) if the activities involved are not substantially the same even with the imposition of conditions; or (b) where registration in one state should not entitle registered persons to carry on a particular activity in another state where (a) that activity is a material part of the practice of a person registered in the first state, and (b) the activity if carried out by a person not conforming to the appropriate standard could reasonably be expected to expose persons in the other state to health and safety risks, and (c) it is not practical to protect the health and safety of persons from that threat by regulating the manner in which services in the occupation are to be provided.

31. There are four agreements between Australia and New Zealand involving standards and certification:

- Under ANZCERTA, the 1988 Memorandum of Understanding on Technical Barriers to Trade restated an earlier commitment "to examine the scope for harmonization of technical requirements such as standards and to encouraging such activity by relevant organizations".
- Under the GATT Agreement of Technical Barriers to Trade, of which both countries are signatories, the transparency provisions oblige advance notice of technical regulations, so as to provide the opportunity to consult in case of difficulties foreseen.
- Under the Australia - New Zealand Agreement on Standards, Accreditation and Quality (ASAQ) signed in 1990, authorities in both countries are required "wherever possible to develop uniform standards based on international standards and to give mutual recognition to test results relating to accreditation and certification activities provided by competent bodies".
- Under the "Joint Accreditation Scheme of Australia and New Zealand (JAS-ANZ) signed in 1991 a joint mechanism was established "for accrediting bodies which will undertake or provide for conformity assessment services", and the agreement facilitates "the harmonization of conformity assessment structures, including quality management systems certification, product certification, laboratory accreditation and personnel certification in New Zealand and Australia. JAS-ANZ also accredits second and third party certification bodies which provide conformity certification systems based on internationally recognized standards."

B. European Community (EC)

32. In the field of personal competence, progress has been made in the EC in recognizing diplomas and qualifications, either by harmonizing the training itself, or through mutual recognition whereby all but a few differences are accepted. However, such is the sensitivity of the regulations affecting the professions that unanimity of decision is necessary among the member States for directives which amend "the existing principles laid down by law governing the professions with respect to training and conditions of access for natural person" (Treaty of Rome, Article 57). Legal requirements affecting professional services in the EC are summarized in Box 4.

33. It took many years to agree upon the few existing harmonization directives, which provide for mutual recognition of full professional qualifications (in the case of architects it took 17 years), and even then the content but not the length of syllabuses was agreed for the medical professions, and the length of education but not the content for architects. Engineers and lawyers could not agree on either length or content. In the case of licensed auditors, the syllabus content was laid down, but not the level of knowledge to be demonstrated (see Boxes 5 and 6 for more information on harmonization in the area of statutory audit in the EC). In order to complete the Single Market in the agreed time scale, the European Commission had to give up introducing such harmonization directives for specific professions, although it will relent in the case of lawyers, who have agreed on the draft of a directive for the establishment of lawyers. Instead it decided to pursue the mutual recognition approach in the two General Diplomas directives which apply to all regulated activities in this field not already covered by harmonization directives. These deal with the recognition of the first three years of university-level education, giving exemption from part or all of the professional education, but in many cases this does not give full professional recognition for those professions which do not have their specific directives (e.g. accountants, engineers, lawyers, planners, and many others): various adaptation and testing procedures are needed for that final stage of acceptance. Only one of the EC directives extends home country control over the supply of services into the host member State, while all other matters remain entirely in the hands of the host country. Non-EC nationals are

Box 4
Legal requirements affecting professional services in the EC

The competence to grant nationality is controlled by member States, subject to international agreements. There is a right of entry for all Community nationals holding a passport or identity card, without the need for a visa, and professionals can transport their equipment if holding a "movement certificate". There is also a right of residence, but only for three months and subject to public health and security policies. This can be extended where an occupational activity is being pursued, for example, of a professional firm, and there is a right to remain upon retirement from employment. There is a right of eligibility for employment, so work permits are not required, and the terms of employment have to be the same as for nationals, including professional conditions.

Employers may not discriminate against a professional on grounds of nationality, while as an employee the professional is subject to the same obligations as nationals. This still leaves open the problem of being discriminated against on grounds such as education, training and qualifications, and the Community directives aim to prevent such discrimination. Non-nationals are not yet on a fully equal footing for employment because eligibility for certain public posts is restricted, which includes the judiciary and some posts requiring professional qualifications.

When making working visits, self-employed professionals cannot be required to join a professional organization in the host country, but they must possess a qualification, attested by a diploma or other formal evidence, awarded by, or recognized as its equivalent by, the host State - this is the right of "Prestation de Service" (cross-border supply of services). A member State may not require a professional to give proof of knowledge of a particular language or to take a language examination, but adequate knowledge of a language may be required under a code of conduct of a profession by which the professional is bound when intending to practise. Professional codes may include many other restrictions on practising, including the taking of an oath and proof that the individual is not bankrupt, and member States may set up information services which have to be contacted about such professional requirements.

The self-employed professional who becomes established has a right to pursue his activities in the host State, with the exception of certain legal and notarial activities, and this has to be under the same conditions as its nationals. This may involve, in some professions, proof of knowledge of a particular language or of local law. The auditing activities of accountants are subject to company law regulations, and may not be carried out cross-border.

The co-ordination of legislation by Community directives affecting the professions mainly covers conditions for their education and training, as a prerequisite for the recognition of diplomas, but a distinction is drawn between the professional title and the training title. In the event of mutual recognition, the professional may use the professional title of the host country, and in addition the training title of the home country described in its language.

As a community national, the professional has these outlined rights of entry, residence and employment - though the latter excludes many public posts such as in the judiciary and others which may require professional qualifications.

There is also the right to self-employment, but there is one set of conditions for a temporary stay to give a one-off service, and another if a local practice is established, when all the local national laws and professional codes apply in full.

Note: Under the European Free Trade Association there were no mutual recognition agreements, and EFTA members are now working on how to adopt the whole set of EC harmonization and mutual recognition directives for the professions, as part of the preparations for the entry into force of the European Economic Area.

Box 5
Statutory Audit the European Community

Although big strides have been made towards the single market within the EC, in the view of the accountancy profession there are still many shortcomings and gaps, because the regulations affecting their activities and profession in the member States remain very diverse, and the 'European accountant' does not exist. For instance there are over 20 different professional profiles at the highest level of qualification, and almost 40 if all levels are considered.

One of the oldest activities of the accountancy profession is the statutory audit, and in the EC both national and community legislation confirm the obligatory nature of such audits and the allocation of responsibility for it to professional accountants alone. In Community law several directives address this activity, and more are proposed. The task assigned to statutory auditors is the same throughout the EC, and is the only activity of accountants for which the same label covers an identical reality in all 12 member States. However, the financial statements of companies upon which the professional statutory auditor should express an opinion are not the same, and in some areas of accounting existing directives do not deal with the accounting treatment. Furthermore the directives contain many options, permitting divergence between member States in areas which are in principle harmonized. Auditors' opinions have to be interpreted solely in the context of the specific national regulatory environment.

Statutory audit is thus the only activity of the accountancy profession subjected specifically to EC law, while all other activities remain unaffected and retain their original characteristics deriving from the law of each member State, and therefore there is no single market. It should be noted also that the eighth directive did not deal with the right of accountants to establish themselves and to practise within the EC. Accountants are subject to the first diploma directive for this.

The operation of these two directives can be seen as abiding by four principles:

(a) A professional authorized in one member State to carry on a profession or regulated activity is also qualified to do so in another member State. Qualifications are in principle equivalent, and any differences can be dealt with by partial re-qualification to overcome significant differences

(b) The level of qualification is evidenced by the length of the period of study, resulting in a stratification of four levels (under 1 year, 1-3 years, 3-4 years, and over 4 years)

(c) The way in which regulated activities are divided or allocated between the different professions, and the manner in which these are regulated, are largely the same, and differences need not be compensated for, other than by the partial re-qualification route mentioned in (a), and

(d) Regulated services in a member States can only be provided by individuals authorized for that purpose in that country. Thus a professional from another member State must adapt to those regulations, which may include compliance with professional rules of a technical and ethical nature - involving effective establishment - and only provide the same services as local professionals.

The directives carefully avoided changing the way in which the professions and regulated services are organised in the member States. They are solely aimed at enabling individual professionals to circulate more easily from one member State to another.

Box 6
The eighth company law directive and statutory audit

The eighth company law directive (84/253) of the European Community lays down conditions for both firms of auditors and individual professionals. However, it does not deal with the independence or professional liability of the statutory auditor. As well as the normal requirement of integrity, it defines the qualification required, and the individual should have "attained university entrance level, then completed a course of theoretical instruction, undergone practical training and passed an examination of professional competence of university final examination level organised or recognized by the State". The directive also lays down a list of subjects which should be specifically covered by test of theoretical knowledge, including examination. The directive is quite precise and exhaustive as regards the topics to be mastered by statutory auditors, but on the contrary remains very vague as to the minimum level of knowledge required in these subjects. There are differences in member States as to what constitutes a "university final examination level".

The directive defines conditions to be respected in order to authorize firms to carry out statutory audits in a member State. Three requirements have to be met at the same time: individual professional auditors must satisfy the conditions laid down, hold the majority of voting rights in authorized firms, and be in the majority on the administrative or management body of such firms. Member States have to maintain registers of authorized professionals and publish lists of their names and addresses.

This directive should have entered into force on 1 January 1990, but implementing legislation is not complete in each member State, and in some member States its implementation has been linked with the first diplomas directive (89/48) which covers accountants, since they do not have their own harmonization directive, as do architects (and the medical professions).

Two approaches have been taken: some member States maintain a specific functional title relating to the carrying out of statutory audits (the course preferred by the accountancy profession), where the title relates to the requirements of the eighth directive only. Thus anyone without this title, using a different professional title, performs all other activities of the profession, but not statutory audits. Such 'registered auditors' would not be members of a specified professional organization, but would be those individuals with this title registered by the authorities. The title would be used alongside the normal educational title (such as chartered accountant). Other member States have chosen not to introduce a functional title for statutory auditing, and the normal professional educational title is the authorization. This in turn affects how the first diploma directive is operated. Implementation of the eighth directive has caused some member States to create new differences, by establishing lower professional levels for small firm audits, or by varying the length and content of the education and training of the two levels.

Box 7

Mutual recognition in the accountancy profession: Canada and the United States

Prompted by the FTA and a common commitment to eliminating impediments to reciprocity, the American Institute of Certified Public Accountants (AICPA), the Canadian Institute of Chartered Accountants (CICA) and the National Accountancy Standards Boards of America (NASBA) achieved a consensus on principles for reciprocity. Implementation, however, depends on the accountants' institutes in the 13 Canadian provincial and territorial jurisdictions, and the state boards of accountancy in each of the 54 US jurisdictions, and would involve granting CPAs from the US a designation in Canada, and for CAs from Canada a designation and license to practise in the US.

Such recognition is based on education, examination and experience. In Canada the requirements to qualify as a CA to practise public accounting includes passing the Uniform Final Examination, essentially the same for each province, and there is reciprocity from province to province, except for Quebec which requires a working knowledge of the French language. In the US requirements vary among the jurisdictions, and the only common requirement in each is the use of a uniform CPA examination. After mutual review by AICPA/NASBA and CICA, it was concluded that the CA and CPA designations are comparable when the examination requirements are combined with the education and experience requirements described below. Subject to these requirements, the basis of reciprocal recognition of the CA and CPA designations would be success in the US Uniform CPA Examination, and certification and licensure by a state board of accountancy, and success in the Canadian Uniform Final Examination (UFE) and admission to membership in a provincial institute of CAs, respectively.

When seeking reciprocity, the individual's educational credentials would be accepted, and the appropriate body of knowledge would be deemed to have been acquired. The applicant would not have to resit the relevant uniform examination. However, all applicants would be required to pass examinations designed to assure that they have "satisfactory knowledge of relevant local and national legislation, standards and practices in the jurisdiction being entered". Such tests for applicants from other jurisdictions are already in place in Canada, but still have to be developed in the US. These examinations may test applicants on the statutes, regulations and ethical rules of that jurisdiction.

As time goes by, the relevant authorities in each country will periodically review in the other the uniform examinations, the body of knowledge tested, administration, security and oversight involved.

As to experience, it was agreed that an applicant could be required to have completed a minimum period of accounting experience under the supervision of a qualified CA or CPA in his original jurisdiction, and if this is adjudged not to meet its requirements the host body can require the completion of prescribed experience in the jurisdiction into which entry is sought.

not covered by the harmonization and recognition directives. It should be noted that the harmonization and general diplomas directives deal solely with recognition of the documentation held by individuals, but not the activities that professionals may undertake, nor how their behaviour is regulated in practice.

C. The Canada-United States Free Trade Agreement

34. The Canada-United States FTA contains specific provisions on licensing and certification of professional services. Despite early progress by the architects within the FTA framework, it is accountants who now appear to be making the most of the FTA through an agreement between the two professional institutes and the United States regulatory board (see Box 7 above). Here mutual recognition of the two professional qualifications is based on agreement as to what is common in their education, experience and examinations, and then testing by examination for differences to ensure applicants have "satisfactory knowledge of relevant local and national legislation, standards and practice in the jurisdiction being entered". After registration, the applicant is subject to host-country control, i.e. national treatment.

35. When the FTA was signed, it was assumed that architects would be in a position to make recommendations for mutual recognition procedures on or before 31 December 1989, because for some time they had independently been engaged in that very process. However, completion has not yet been achieved, probably due to failure of the US states to agree to the equivalence of school accreditation and examinations.

36. The lessons which appear to be drawn from this experience are that mutual recognition is a complex endeavour, particularly when carried out by federal states, and it is a very time-consuming process, made longer by the involvement of sub-national entities. This may lead Governments to encourage the professions to take over responsibilities of accreditation from them. Lack of progress can also be ascribed to lack of resources, both human and financial, available to the professional associations to complete the mutual recognition processes. However, a positive step forward has now been made by the accountancy profession, as described here. It is expected that the first examinations to be held under the mutual recognition arrangement could take place later in 1993. The joint body could also fulfil the role of investigating the situation of third-country professionals who apply for recognition.

D. North American Free Trade Agreement (NAFTA)

37. Although, under NAFTA, the principle of national treatment will apply, it is proposed to take a further step by building in procedures "for the processing of applications for licenses and certifications", and "the development of professional standards" in the case of people who are licensed to practise or whose practice activities are restricted by law. This will include procedures for temporary licensing. However, there are no obligations at this stage, only a generic blue-print to encourage the professions to reach mutual recognition agreements. The emphasis is on the professions being fully involved in the process under a framework laid down by Governments. There is also provision for temporary entry under simplified procedures of business persons in four categories, of which one comprises professionals. This is likely to be an advance on what can be agreed in the counterpart annex of the GATS. Some activities are being excepted, as are initially some professions.

38. NAFTA includes a Chapter 12 entitled "Cross-Border Trade in Services" which applies to measures relating to cross- border trade in services, including their "production, distribution, marketing, sale and delivery"; "the purchase or use of, or payment for, a service and some other financial aspects; access to distribution and transportation systems; and also "the presence [...] of a service provider" [1201 (1)].

39. Chapter 12 does not apply to financial and air services (in the main), nor to public procurement, or state subsidies and grants. It imposes no obligations

with respect to people seeking access to an employment market, or employed on a permanent basis. [1201 (2 and 3)] Chapter 16 deals with "Temporary Entry for Business Persons", which includes the professions (see below). Presence in the market through investment is dealt with in Chapter 11, sub-chapter A, "Investment": the "cross-border provision of a service or cross-border trade in services does not include the provision of a service in the territory of a Party by an investment". [1213] The cross-border provision and trade in services is defined in essentially identical terms as trade in services is defined in the draft GATS. [1213]

40. The principal obligations are to accord national treatment ("treatment no less favourable than that it accords to its own service providers") and most-favoured-nation treatment (MFN) ("treatment no less favourable than that it accords to service providers of any other Party or of a non-Party") [1203/4]. A service provider may not be required "to establish or maintain a representative office or any form of enterprise, or to be resident as a condition for the cross-border provision of a service" [1205 Local Presence]. Existing non-conforming restrictions can be maintained (i.e. grandfathered) at the federal, state or provincial and local government levels but have to be listed in a schedule within two years - though not those maintained by a local government. Both Canada and the United States have entered reservations for existing nationality and citizenship requirements affecting patent attorneys and agents. However such restrictions have to be phased out within two years under the provisions of 1210 (3). Mexico has entered a number of reservations affecting medical doctors, veterinary doctors, lawyers, notaries, accountants and other professional services. Some of these non-conforming restrictions are not to be phased out. There is also provision to omit "sectors, sub-sectors or activities" from the obligations on national treatment, MFN and Local Presence [1206]. Any quantitative restrictions have also to be scheduled [1207].

41. "Commitments to liberalize quantitative restrictions, licensing requirements, performance requirements or other non-discriminatory measures" have to be scheduled [1208]. Article 1210 is headed "Licensing and Certification", wherein the Parties "shall endeavour to ensure that any measure "relating to the licensing or certification of nationals of another Party" is based on objective and transparent criteria, such as competence and the ability, is not more burdensome than necessary to ensure the quality of a service, [and] does not constitute a disguised restriction on the cross-border provision of a service".

42. There is an annex entitled "Professional Services" [1210.5] which deals with the "processing of applications for licenses and certifications" and the "development of professional standards". "Professional services" means "services the provision of which requires specialized post-secondary education, or equivalent training or experience, and for which the right to practise is granted or restricted by a Party, but does not include services provided by trade-persons or vessel or aircraft crew members". The Annex for professional services states that "The Parties shall encourage the relevant bodies in their respective territories to develop mutually acceptable standards and criteria for licensing and certification of profession service providers and to provide recommendations on mutual recognition". It then gives a detailed list of the matters which should be addressed when developing standards and criteria, including knowledge, experience, ethical conduct, scope of practice, and consumer protection [1210.5 Section A (2 and 3)]

43. On temporary licensing, "where the Parties agree, each Party shall encourage the relevant bodies in its territory to develop procedures for the temporary licensing of professional service providers of another Party". [1210.5 Section A (5)]. This Annex has a section entitled "Foreign Legal Consultants", which obliges parties who have made relevant commitments to "ensure that a national of another Party is permitted to practise or advise on the law of any country in which the national is authorized to practise as a lawyer" [1210.5 B (1)]. A Party has to "consult with the relevant professional bodies to obtain their recommendations on the form of association or partnership between lawyers authorized to practise in its territory and foreign legal consultants, the

development of standards and criteria for the authorization of foreign legal consultants, and other matters". [1210.5 B (2)] On future liberalization: "Each Party shall establish a work programme to develop common procedures throughout its territory for the authorization of foreign legal consultants" [1210.5 B (4)].

44. A further section of the Annex is entitled "Temporary Licensing of Engineers". "The Parties shall meet within one year of the date of entry into force of this Agreement to establish a work program to be undertaken by each Party, in conjunction with its relevant professional bodies, to provide for the temporary licensing in its territory of nationals of another Party who are licensed as engineers in the territory of that other Party". [1210.5 C (1)] Consultation with those professional bodes is to obtain their recommendations on such matters as "procedures for the temporary licensing of engineers", "the development of model procedures to facilitate temporary licensing" and "engineering specialties to which priority should be given" for this. [1210.5 C (2)] These engineering bodies are to be encouraged to meet "at the earliest opportunity" and shall be requested to submit "an annual report on the progress achieved". [11210.5 C (4)] (In Mexico, this is limited to Civil Engineers.)

45. An annex to the chapter on temporary entry of business persons covers four categories: business visitors, traders and investors, intra-company transferees, and professionals, who only have to undergo minimal paperwork requirements, and no labour certification tests [Annex 1603]. The section on professionals [annex 1603 D] obliges each Party to "provide confirming documentation to a business person seeking to engage in a business activity at a professional level" in a specified list of 63 professions. These persons have only to demonstrate the educational requirements or alternative credentials specified for each profession, at least at a university degree level. Numerical quotas can be set, and the United States has imposed a limit of 5,500 for the entry of Mexican professionals on top of its existing limits, but Canada has not done so.

46. Chapter 16 establishes a trilateral working group which will devise general improvements which might include in this field expanded coverage for professionals and temporary entry benefits for spouses. Chapter 11, "Investment", covers all types of investments and investors (unless covered by Chapter 14, "Financial Services") and lays down NT and MFN obligations "with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments". It specifies various performance requirements which are banned. It does permit requirements that a majority of the board of directors, or any board committee, of an enterprise be nationals or residents.

E. Mercado Comun Sudamericano (MERCOSUR)

47. The Treaty of Asuncion was signed on 26 March 1991 between Argentina, Brazil, Paraguay and Uruguay, with the aim of creating a common market by 1 January 1995. It provides for the free movement of capital, goods, services and people, a common external trade policy and tariffs, and the co-ordination of macro-economic policies. The governing body is the Common Market Council, composed of the Ministers of Finance and Foreign Relations, and its permanent secretariat is in Montevideo, Uruguay. Ten working groups deal with various issues, and include harmonization of internal trade legislation, maritime and land transport, and intellectual property rights protection.

48. On 26 March 1992 the Argentine and Brazilian Bars negotiated a co-operation agreement aimed at being a model and a start towards the integration of legal services in the Mercosur. In June 1992 a protocol of judicial co-operation was signed aimed at improving the enforcement of orders of courts of one country in the others. The Brasilia Protocol established dispute settlement procedures in the legal field by means of direct negotiations, conciliation and arbitration, available for the four Governments and private parties.

49. Argentina and Brazil have also ratified the statutes of a form of bi-national company granting companies incorporated in one jurisdiction equal

legal treatment with those incorporated in the other. Work has still to begin on the right of establishment (and non-establishment) for service industry firms.

Box 8
Right of lawyers to establish in Brazil

The legal profession in Brazil is regulated by a federal statute enacted in 1963. It established the Bar Association as responsible for the admission, discipline and defence of lawyers, and it laid down the organization and procedures for it, including in each state. Only persons registered with the Bar Association may practise law and use the denomination 'lawyer'. Eligibility for membership of the Bar rests on certain civil and moral requirements, the ownership of a bachelor or doctorate degree in law and a certificate of clerkship and bar examination pass. A foreign lawyer can be admitted to the Bar where the same facility is available in the foreigner's country of origin and the presentation of a revalidated diploma, if the applicant did not graduate from a Brazilian law school.

The services of a lawyer are defined by the statute and include representation of a client in any court or tribunal, including administrative ones, procuratorship, counselling, and advisory services, and the work can consist of drafting complaints, pleas, replies, petitions, briefs and drafts for judicial proceedings, as well as acting in the defence for proceedings in any court or jurisdiction. Others working in the legal profession such as solicitors, law clerks and para-legals may not perform these prescribed services, and their work is also laid down in detail. Nor may law firms perform acts reserved to individuals, i.e. lawyers admitted to the Bar.

It is a criminal offence for any member of the profession to advertise. The name of a firm must include at least one of the lawyers who is a general partner, and is a member of a local section of the Bar, and must not include anyone prohibited from practising law. However, non-lawyers can be partners in a law firm, including law clerks.

In an agreement between Brazil and Portugal, a lawyer who is a Brazilian national, graduating from any law school in Brazil may practise in Portugal, under a Portuguese executive law of 1984, and any lawyer who is a Portuguese national granted a diploma by a Portuguese law school, may become a member of the Brazilian Bar, as long as the lawyer observes the registration requirements of both the Brazilian and Portuguese regulations.

The Brazilian Bar has not yet regulated the position of Foreign Legal Consultant (FLC), as has been done at the New York Bar and a number of other US states, in EC directive 77/249/EEC, and in Japan.

One solution being advocated by a distinguished Brazilian Bar Association member would provide for the separate registration of an FLC for the purpose of giving advice on the laws of his own jurisdiction, where he is authorized to practise, whilst resident in Brazil. The Bar would satisfy itself that the lawyer had been admitted to his native Bar on the basis of its certificate, that the applicant had not been convicted of a crime, was of good conduct, agreed to observe the standards laid down by the Bar for FLCs, and maintained a liability insurance policy, a copy being filed with them.

The FLC would not be permitted to advertise the registration, or to be a member of the Bar, and would be expressly forbidden from rendering services reserved or restricted to a Brazilian lawyer, including advocacy. The FLC would be subject to periodical reviews of conduct and ethics, and at the outset certify having read the Code of Conduct of the Brazilian Bar, and thereafter notify the Bar of any penalty imposed by the Bar of origin. The certificate of registration would be suspended or revoked by the Bar if any of the requirements were not complied with.

F. Brazil/Portugal agreement on lawyers

50. An example of mutual recognition of professional qualifications is found in the case of the agreement between the Governments of Brazil and Portugal, under which graduate lawyers may practise in either country, but they have to observe both home and host country control. Many lawyers argue that given the special characteristics of their profession make a specific consideration of their sector necessary, and they wish to focus first on ensuring that foreign lawyers in the host country can give advice on their home country law and on international law when it refers to a third country. See above, Box 8, for more information on the right of lawyers to establish in Brazil.

G. Draft General Agreement on Trade in Services (GATS)

51. The draft General Agreement on Trade in Services (GATS) does not provide for the Council on Trade in Services to become a licensing body, but it does state that it will "through appropriate bodies it may establish, develop any necessary disciplines" to ensure "that measures relating to qualification requirements and procedures, technical standards and licensing requirements do not constitute unnecessary barriers to trade" (Article VI). Article VII encourages recognition of the education or experience obtained, requirement met, or licenses or certification granted in a particular country, which may be achieved through harmonization or otherwise. It also obliges Parties to improve transparency in domestic rules, regulations and measures affecting services which are relevant to the Article, and sets out the objective of establishing and adopting, in co-operation with relevant intergovernmental and non-governmental organizations, common international standards and criteria for recognition and common international standards for the practice of relevant services trades and professions. Moreover, Article XVIII of the draft GATS encourages Parties to negotiate "additional commitments" with respect to measures affecting trade in services not subject to scheduling under Articles XVI "Market Access" and Articles XVII "National Treatment", including those regarding qualifications, standards or licensing matters. The Council will also monitor recognition agreements between signatories, all of which have to be registered with GATT and be "based on multilaterally agreed criteria" (Article VII).

52. In the negotiation on initial commitments on trade in services, recognition of qualifications and practical experiences have been raised for a variety of sectors, including accountancy, architectural services, engineering services and legal services.

VII. Conclusions and recommendations

53. Professional services are highly regulated in respect of qualification requirements, technical standards and the range of activities which practitioners conduct. Professional associations were formed to assure their members' standards of professional competence, ethical behaviour and personal accountability, and they influence entry to professions and standard-setting in their countries. The prevalence of complex regulations and procedures on qualifications and standards can be an obstacle to the effort to export professional services, and the difficulty is aggravated to the extent that these regulations and procedures are less than transparent. The Uruguay Round negotiations on trade in services discussed the problems of market access and national treatment for professional services in this respect. The draft GATS, in Article VII, addresses the issue of recognition and harmonization of qualifications and sets out the objective of establishing and adopting common international standards and criteria for recognition and common international standards for the practice of relevant services trades and professions, while Article XVIII provides the possibility of additional commitments in this area. Also, recognition of qualifications and practical experiences for accountancy, legal services and architectural and engineering services have been requested by some negotiating countries in the Group of Negotiations on Services.

54. Some initiatives have been taken, in the context of regional economic integration agreements, to recognize and harmonize qualifications relating to professional services. Experience in negotiating harmonization and recognition of qualifications indicates that such processes should cover the body of knowledge, examinations, codes, and enforcement procedures, as well as standard-setting factors such as education and training requirements, and structure of services. Some professional services require intimate local knowledge of legal, economic and geographical environments, and qualifications systems and standards are designed to meet these requirements, as well as universally required knowledge. In the process of harmonization and recognition, therefore, maintaining minimum standards and local knowledge requirements is a key aspect. The EC has been dealing with the issue for nearly 20 years, but the scope of recognition and harmonization is still quite limited, demonstrating the complexity of the process involved. The Canada-United States Free Trade Agreement is close to implementation for accountancy. However, none of the other regional trade agreements which deal with harmonization and recognition of qualifications among the signatory countries have come to the implementation stage.

55. Professional services are governed by regulations and measures which concern aspects other than professional competence such as establishment of legal accountability, foreign-exchange management and protection of cultural and national objectives. The multilateral negotiations on trade in services identified various regulations and measures governing professional services as barriers to liberalize their trade. These include: (i) residency requirements; (ii) visa and work permit requirements; (iii) restrictions concerning establishment and scope of activities; (iv) restrictions on transborder data flows; (v) restrictions on capital transfer; (vi) prohibition on non-nationals obtaining local qualifications; (vii) restriction on the use of an international firm name; (viii) tax discrimination; (ix) discriminatory licensing of firms; (x) prohibition of foreign-produced broadcast material; (xi) favouring of local agencies in government procurement; (xii) restrictions on staff that can be employed; (xiii) discriminatory regulation of fees and expenses; (xiv) use of subsidies or other forms of official support being granted to domestic suppliers. In eliminating barriers to trade in professional services, these regulations and measures need to be assessed thoroughly in terms of their justification so that the legitimate objectives of consumer protection, civil liability, cultural protection and economic development are respected. This would allow countries to participate actively in the efforts to promote harmonization and recognition of qualifications and standards.

56. There is only limited information available on how trade in various professional services actually takes place. Up to now, the issue of harmonization and recognition of qualifications has focused on free movement of professionals across borders. However, in professional services such as accountancy, it appears that the movement of relatively few accredited professionals occurs, and the majority of the work involved is conducted by local personnel or via transborder data flows or the movement of some support staff in critical situations. On the other hand, for trade in construction and engineering services, although actual movement of accredited professionals is relatively marginal, recognition of qualifications has important implications for firms in obtaining contracts. Lack of information on the forms of trade in professional services also impedes efforts to assess how the regulations and measures referred to above are affecting such trade. A further study might address forms of trade in professional services to evaluate more precisely how regulations and measures, including the ones relating to qualifications and standards, are affecting their trade. Understanding the relevance of harmonization and recognition of qualifications to different professional services will facilitate the identification of priorities in that respect.

57. In order to identify clear policy courses at the national and international levels the questions to be addressed include: (i) what are the priority services for harmonization and recognition of qualifications; and (ii) what are desirable policy courses for developing countries in dealing with the issue of

harmonization and recognition of qualifications. In this connection, inputs from professional associations are indispensable. However, there is limited information, except for accountancy, as to how existing relevant professional associations view the issues of harmonization and recognition of qualifications. In the case of accountancy, professional associations are actively involved in harmonization and recognition of qualifications and standards at the international level. This is partly due to their international exposure from an early date and the existence of global networks.

58. The Standing Committee could seek the co-operation of member Governments to provide information regarding professional associations in their countries, i.e. their names, addresses, aims, procedures and involvement in recognition and harmonization of qualifications. The Standing Committee might wish to invite major international and regional professional associations to make submissions on the key issues arising in harmonization and recognition of qualifications and seek their views as to how UNCTAD could assist in this area. Also, the Standing Committee might wish to study the benefits which would accrue to developing countries from the development of multilateral procedures in harmonization and recognition of qualifications so as to recommend policy courses for these countries. The data base on measures affecting trade in services envisaged under paragraph 2 (b) of the work programme of the Standing Committee could give priority to the inclusion of services generally subject to licensing and certification requirements.

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THE IMPACT OF SUBSIDIES ON TRADE IN SERVICES

Background Note by the UNCTAD Secretariat

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INTRODUCTION

1. Under item 3(d) of its Work Programme, the Standing Committee on Developing Services Sectors will study the impact of subsidies on trade in services, especially on the exports of developing countries. The secretariat has prepared this note with the objective of providing elements which could assist the Standing Committee in its further consideration of this issue.

2. The multilateral trading system has traditionally had difficulty in coming to grips with the issue of subsidies, reflecting to a large extent differing perceptions among countries as to the appropriate role of governments in the support of economic, social and development objectives, and the acceptability of the trade effects of the pursuit of these objectives. The original text of GATT contained few disciplines on subsidies (although the industrialized countries soon recognized the need for special disciplines on export subsidies), and the approach was to focus on the effects of subsidies, with respect to both import replacement and impact in export markets. Dispute settlement action could be initiated if subsidies were deemed to cause serious prejudice to other contracting parties.

3. Material injury to domestic industries caused by imports of subsidized products may be and has been countered though the imposition of countervailing duties. The perceived abuse of countervailing duties as a means for trade harassment, and the unwillingness of some countries to accept tighter rules governing their application without corresponding disciplines on subsidies, led to the negotiation of the Tokyo Round Code on Subsides and Countervailing Duties. However, while intensifying the rules on export subsidies, this instrument was ineffective in clarifying rules on subsidies in general, although it recognized that subsidies were an inherent part of economic development programmes of developing countries. The Code was accepted by only a minority of GATT contracting parties. It was decided to renegotiate the Code in the Uruguay Round. The resulting Agreement on Subsidies and Countervailing Measures in the Draft Final Act appears, for the first time, to reflect an international consensus as to what forms of subsidies are acceptable. It classifies subsides into "prohibited", "actionable" and "non-actionable" categories, and further tightens the disciplines governing the application of countervailing duties. While it is envisaged that the Agreement would apply to all GATT contracting parties, including the many developing countries which did not adhere to the Tokyo Round Code, more specific provisions for differential and more favourable treatment for developing countries have also been incorporated into this instrument.

4. The fact that these fundamental conceptual problems were still being worked out with respect to subsidies on trade in goods, the absence of adequate information or past experience with respect to subsidies on services, the recognition that subsidies on services might take different forms and give rise to different problems than those on goods, and that trade in services was effected through four modes of delivery, were likely among the factors which led the Uruguay Round negotiators to postpone attempts to agree upon disciplines on subsidies on trade in services in the General Agreement of Trade in Services (GATS). Article XV of GATS recognizes that subsidies may have distortive effects on trade in services, and provides that the parties shall enter into negotiations with a view to developing the necessary disciplines to avoid such trade distortive effects, in the context of a future work programme. These negotiations will also address the appropriateness of introducing countervailing procedures and recognize the role of subsidies in relation to the development programmes of developing countries and the needs of developing countries for flexibility in this area. For the purposes of such negotiations, the parties

shall exchange information concerning all subsidies related to trade in services that they provide to their domestic service providers.[1/]

Chapter I

SUBSIDIES FOR THE SERVICES SECTOR

5. International consensus on what constitutes a "subsidy" has consistently eluded the international trading community. The Agreement on Subsidies and Countervailing Measures included in the Uruguay Round Draft Final Act comes closest to achieving that consensus. The essence of the DFA definition is that the subsidy should result in a benefit being conferred through a financial contribution by a government (whether or not effected through a private body), including direct payments, or by the government foregoing revenue otherwise due, or by providing goods and services other than general infrastructure, by the government purchasing goods, or through income or price supports. Such subsidies are prohibited or actionable only to the extent that they are specific in the sense that they are limited to certain enterprises. The characteristics of goods and services being different, this definition, drawn up with trade in goods in mind, may not be entirely applicable to trade in services.

6. It should be noted in this context that an important type of subsidy to the trade and production of goods is the provision of services by the government under more favourable conditions. Subsidies to services act as subsidies to the production and export of goods and vice versa. The provision of subsidized services has led to countervailing actions against exports of the goods using or incorporating such services. Subsidies to goods could thus also be considered to provide subsidies to services, as is discussed below.

7. The DFA Agreement on Subsidies and Countervailing Measures, building upon elements of the Tokyo Round Code and GATT article XVI, already addresses certain services. For example, the preferential provision of internal transport and freight on export shipments, provided or mandated by governments on terms more favourable than for domestic shipments, constitutes a prohibited export subsidy.[2/] On the other hand, government assistance to consultancy services used for research purposes is considered a non-actionable subsidy.[3/] A variety of services, including infrastructural services to the agricultural sector, are exempted from the reduction commitments generally applying to domestic support for agricultural production.

8. In practice, input and infrastructural services have been alleged or determined as constituting "countervailable" subsidies in many countervailing duty investigations,[4/] including: (a) the provision of utilities at lower rates

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[1/] It should be noted that in GATS the two most important subjects where the negotiation of precise disciplines were postponed - i.e. subsidies and safeguards - are precisely those where in GATT multilateral obligations are related to judgements of economic impact of trade measures.

[2/] The Uruguay Round Agreement on Agriculture subjects such measures to a specific reduction commitment, although developing countries are exempted from this commitment until 1999.

[3/] Article 8 defines "applied research" as including work for the creation of new products, production processes and services.

[4/] These samples have been drawn from the experience of the United States on account of the availability of published information.

when used in production for export;[5/] (b) government-financed construction of infrastructures, including storage and processing facilities, for export-oriented industries;[6/] and (c) preferential rates for government-owned transportation for exported products.[7/]

9. It should also be recalled, however, that the same DFA has established a definition of trade in services that can be considered somewhat broader than that of trade in goods. Notably, such trade can be effected through commercial presence and the movement of natural persons to supply services as well as the movement of consumers. This implies that benefits accruing to enterprises (in the sense of Article 1 of the Subsidies Agreement), such as preferential tax regimes for foreign operations, which directly or indirectly benefit their foreign-based subsidiaries might also be considered as subsidies to exports of services. In addition, subsidies to the parent firm in the home country could provide competitive advantages to foreign subsidiaries abroad. Government programmes which underwrite costs of foreign travel to provide services could also conceivably be considered as export subsidies. Special fiscal and other benefits in favour of foreign consumers who purchase services in the country might also fall in this category. As noted below, the application of GATT principles for border tax adjustments may be particularly complicated in the case of trade in services.

Chapter II

SUBSIDIES TO SERVICES: SOME EXAMPLES

A. Subsidies to Infrastructural Services

10. As has been observed in the note prepared under item 3(a) of the Work Programme, governments have traditionally been faced with the dilemma arising

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5/ An example would be the program providing electricity discounts for exporters, under which Thai exporters received a discount of 20 per cent of the cost of electricity consumed to produce exports. While this program was terminated effective 1 June 1990, the United States Department of Commerce (USDOC) found it countervailable in the instance of steel wire rope from Thailand because of residual benefits. This type of subsidy has also been a major issue in magnesium from Canada.

6/ In fuel ethanol from Brazil, USDOC examined an allegation that sugar cane growers in the Northeast of Brazil have benefitted from plantation roads built at government expense for their exclusive use. While USDOC did not feel that such activities did not constitute a countervailable subsidy, they determined that the programme was not used as none of the respondents was located in the Northeast of Brazil. In certain fresh Atlantic groundfish from Canada, USDOC found numerous Canadian programmes to be countervailable, including: *Federal Programmes:* assistance for the construction of ice-making and fish-chilling facilities; preferential user fees to fishermen under the small craft harbour programme; and *Provincial Programmes:* New Brunswick: fish-unloading systems and ice-making programmes; Newfoundland: grants for rebuilding and repair of fishing and coastal vessels; P.E.I.: engine conversion programme; assistance for the construction of the ice-making and fish-chilling facilities; Quebec: grants for fish transport and seafood processing tanks; ice-making and fish-chilling assistance.

7/ Preferential ocean freight rates were alleged in potassium chloride from Israel but were not proven to the satisfaction of USDOC. In tool steel from Brazil, USDOC declined to find countervailable transportation subsidies from preferential rail rates because the exporters used trucks to move the product to the port of exportation. USDOC reached the same conclusion in certain stainless steel products from Brazil.

from the objective of providing infrastructural services in an efficient manner while, at the same time, seeking to ensure access to basic services for the widest possible proportion of the population, including persons with low purchasing power and persons and enterprises in less advantageously located regions of the country. These considerations have led to policies for subsidization, in particular of transportation and utility services.[8/] In many cases these subsidies are aimed at supporting the establishment or development of particular industries such as fishing, forestry, agricultural production, or natural resource extraction and refining, as well as services such as tourism, and have often been crucial to the development or survival of the industry or service concerned. Where these have been deemed to affect trade in the goods concerned they have sometimes provoked the imposition of countervailing duties by affected trading partners. Such subsidies can have an impact on trade in services when extended to the international arena, notably in the air and maritime transport sectors. The desire to have a national shipping company or airline for strategic or other reasons has led governments to heavily subsidize such operations, whether or not state-owned. There has been considerable documentation of subsidies affecting the maritime transport sector,[9/] such measures including fiscal and non-fiscal subsidization of operating and construction costs (the latter is essentially a subsidy to services through a subsidy to goods as discussed below). Rail transport has also traditionally been a heavily subsidized service sector.

11. Other categories of infrastructural or social services such as education, and often health services, are provided free or at minimal cost by the government. In many cases these services have attained a degree of efficiency and quality such that they can be exported, i.e., sold to foreign consumers in the country of origin, or through domestic enterprises or individual persons which offer such services in foreign countries. In particular, educational and health institutions, which may benefit from a variety of government subsidies, can offer services to foreign clients on a profit basis. Some developed countries are major exporters of educational and health services, through several modes of delivery. In this context, a number of developing countries are attempting to develop exports of specialized medical services as a means of cross-subsidizing the provision of health services to nationals.

12. In the telecommunications sector, subsidization can take the form of (a) government subsidization of telecommunications infrastructure, i.e., to facilitate the provision of a variety of telecommunication services, and (b) subsidization of the users of telecommunications services by government entities themselves, providing such services at less than full cost. The current boom in telecommunications trade has enabled most public telecommunications operators in OECD countries to show higher profits (very few operate at a loss), while actually reducing rates.[10/] For developing countries the situation is different. One of the issues discussed in the Uruguay Round negotiations on services was the extent to which cross-border telecommunications charges should reflect costs, and it was accepted that developing countries could retain their cross-subsidization schemes under which international communications were overcharged so as to provide financing for the development of the national telecommunications infrastructure. Some countries have provided telecommunications facilities at less than full cost in order to attract and

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[8/] United States programmes to support *rural electrification* and rural telephone services were examined by Revenue Canada in their 1986-7 CVD investigation of *grain corn* and were determined to be "normal functions of government" and not countervailable.

[9/] See for example L.J. White, *International Trade in Ocean Shipping Services, the United States and the World* (Cambridge, Mass.) as well as Commission of the European Communities, *Report on United States Trade and Investment Barriers 1992*.

[10/] OECD, *Communications Outlook 1993* (Paris: OECD, 1993).

support the operations of exporters of data processing and other information services. PTTs can also use profits from telecommunications services to cross-subsidize to support postal services which can, in turn, be provided at lower cost to support certain activities (e.g., domestic publications). As telecommunications firms, both public and private are increasingly more active in seeking clients wishing to establish international networks, export subsidization or the non-competitive actions of monopolies might become a more important issue in this sector.

B. Export Market Development

13. An important category of subsidized services are those related to "export market development", which may be sectoral and/or market-specific. Under such programmes, the government provides financial assistance to cover costs of a variety of activities related to the penetration of new markets or the preparation of feasibility studies and project proposals. Such programmes are primarily intended to lead to exports of the final product or service. However, the subsidization of feasibility studies, and the preparation of bids in particular, have been the subject of complaints from engineering and consultancy firms in developing countries, which find that they are not able to compete with subsidized foreign firms, neither in third-country export markets nor in their home markets.

14. The subsidized feasibility study can lead to the export of a major project which may also be subsidized through export credits which can be tied to the purchase of both goods and services from the country of origin.[11/] National donor agencies tend to tie financial support (formally or informally) for the execution of an investment project to the selection of a consulting firm from the donor country. In this context, as in other instances mentioned below, dumping can exist in parallel with subsidization as the firms themselves will often sell pre-investment services below cost in anticipation of gaining large construction contracts, as such services account for only about five percent of the project cost but tend to influence construction contract awards and procurement of equipment and raw materials, which can represent more than 70 per cent of project cost.

15. Developing countries have used various incentive schemes such as tax incentives, banking credits and accelerated depreciation allowances to promote the development of an export capability in engineering and construction services; with a few exceptions, however, they have not been able to compete effectively against the financing packages available to firms from developed countries.[12/] Many developing countries appear to have been reluctant to include construction and engineering services in their offers in the Uruguay Round negotiations, considering that trade in this sector was distorted by subsidies and other anti-competitive practices to such an extent that it would be unwise to enter into commitments to provide market access until more concrete disciplines could be

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[11/] An example of such assistance may be found in the U.S. Department of Commerce review of Canada's Program for Export Market Development (PEMD) in Oil Country Tubular Goods from Canada. This programme provides grants to defray the cost of export market development. The programme applies to exports of goods and services. These grants are repayable if they lead to securing export contracts for services. This type of programme benefits companies whose exports involve bid and proposal preparation. A 50 per cent grant, whether repayable or not, doubles the effective bid preparation market development budget of exporters who use the programme. See 51 FR 15041; 53 FR 50057; 44 FR 61589.

[12/] See Y. Soubra "Construction and Engineering Design Services" in *Trade in Services Sectoral Issues* (UNCTAD/ITP/26), pp. 185-214.

negotiated on subsidies and anti-competitive practices in the General Agreement on Trade in Services.[13/]

C. Media Services

16. Another sector where subsidies are prevalent is that of media services. Film production, advertising, and publishing often receive considerable financial support from governments and are generally available to all cultural industries. These include direct grants for the conception or production of a film, subsidized postal rates, etc. To a certain extent, such subsidies are a response to the peculiarities of trade in media products, such as cinema film in which most of the cost in making the "product" is incurred in turning out the first copy of the film or television programme. Additional copies can be reproduced very inexpensively, and these costs can easily be written off in large homogenous markets, protected by differences in cultural attitudes.[14/] Subsidies or quotas are in essence a response to imports that could technically be considered as having been dumped in the market. Similar situations arise with respect to the editorial content of newspapers and magazines.[15/]

D. Financial Services

17. Subsidies can be provided to the financial service sector through the tax system, primarily the treatment of losses carried forward or back from one tax period to another. In recent years, banks in all industrialized countries have been increasing their loss reserves; how these are taxed or not taken as taxable income is an important consideration for banks and property mortgage firms. More generally, government-financed rescues of financial institutions can be considered as a subsidy to the financial service subsector involved in the country concerned. In the absence of such government funding, the financial institutions themselves would have to absorb all the costs of rescuing a failed firm or incur costs arising from increased lack of confidence on the part of financial service consumers.[16/] Another form of implicit subsidy may be present in national prudential regulations which affect the capitalization of financial service firms. The lower the level of "capital adequacy" provisions, the greater the volume of loans banks can provide, and thus the higher the income they earn for a given volume of capital. This issue has been addressed by the Basle

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[13/] The extent of export subsidization in the construction sector is described by J. Lee in "Construction", in *The Uruguay Round and Services in the World Economy* (New York: World Bank and UNCTC, 1990).

[14/] See Susan Christopherson and Stephen Ball "Media Services: Considerations relevant to Multilateral Trade Negotiations" in *Trade in Services: Sectoral Issues* (UNCTAD/ITP/26). It should be noted that only two per cent of the television programmes in the United States are imported. See Tapio Varis, *International Trade in Television Programmes* (Paris, UNESCO, 1985).

[15/] Recently, a U.S. publication, *Sports Illustrated*, contracted with a Canadian printing/publishing firm to produce an edition for the Canadian market. The editorial input would be produced in New York and transmitted electronically to the printer in Canada. The Canadian publishing industry made representation to Canadian Customs authorities that anti-dumping duties should be imposed. Revenue Canada determined that they could not impose duties on electronically transmitted computer data. Over the ensuing months, this initiative attracted strong reactions from Canadian publishers and advertising industry representatives, and the Government of Canada established a task force to examine the problem.

[16/] See Rodney de C. Grey, "Subsidies on Traded Services, and Possible Offsetting Measures" (mimeo), UNCTAD, Geneva, 1992.

Committee on Banking Supervision which has formulated a set of capital adequacy standards now being put into effect in all major countries.[17/]

E. Subsidies to Goods

18. As noted above, subsidized service inputs have been deemed as constituting subsidies to the production and export of goods and services. Similarly, subsidies to goods can constitute subsidies to traded services. In certain cases subsidies to the service provider are conditional on the use of domestic goods, such as in the area of maritime transport.[18/] A variety of such subsidies related to the production and repair of ships and aircraft and the subsidization of shipping costs can be found in the maritime transport sector.[19/] Similarly, subsidies related to the production and maintenance of aircraft affect competitiveness in air transportation and of airline companies. Soft loans and other assistance to hotel construction can enable countries to improve their competitive position in the tourism market.

19. A similar link arises when services fall under subsidy programmes applied to specific goods exports, such as the case of the subsidies to advertising agricultural products of the United States as part of the United States Export Enhancement Program.[20/]

F. Government Purchases

20. There are areas where the frontier between what is a subsidy, in the sense of a financial contribution by a government, and benefits obtained from other forms of trade protection, notably failure to provide national treatment, is difficult to discern. Government purchases of goods[21/] can be considered a subsidy according to the DFA definition. Government purchases of services, which are extremely important in certain service sectors, could conceivably play the same role if they provide service producers with assured markets that would enable them to reduce their costs so as to compete more effectively internationally. A common example is the requirement that government employees must travel on domestic airlines when on official travel. Government purchases also provide consulting services with a major market - and one in which domestic consultants can cover much of their basic or fixed costs, particularly in periods of economic downturn. This situation provides opportunities for consultants in many disciplines to engage in "cutting edge" research and research and development work. Such assignments, undertaken for governments with considerable infrastructural support, enables these consultants to develop and expand their

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[17/] See UNCTAD, *Trade and Development Report 1992* (UNCTAD/TDR/12), Part Two, Annex I.

[18/] Section 601 of the United States Merchant Marine Act, as amended, provides for the payment of an Operating Differential Subsidy to United States operators of ships built in the United States of United States materials so as to place their operating costs on a parity with those of foreign companies. See Commission of the European Communities, *Report on United States Trade and Investment Barriers 1992*, p. 52.

[19/] See also discussion of subsidies in shipping and shipbuilding above, and boxes 1 and 2.

[20/] See "US Subsidizes Firms' Foreign Ads", *International Herald Tribune*, 25 July 1990.

[21/] The USDOC found such purchases to be countervailable in nitrocellulose from France.

knowledge base and to make their services more valuable and attractive to foreign clients in the commercial sector, and indeed to other governments. [22/]

21. Elements of trade regimes for trade in goods, such as rules of origin provisions which include service inputs in the regional content requirement, can provide special benefits to service suppliers.[23/]

G. Border Tax Adjustments

22. The GATT rules permit the rebate of indirect taxes on exported products and the imposition of taxes on imports to the extent that they are "borne by the like product when they are destined for consumption in the country of production or exportation"; on the other hand, direct taxes and social welfare charges can be assessed only in the country of production and may not be rebated or imposed on imports.[24/] Some countries have applied this principle to services. For example, in Canada foreign consumers are rebated indirect taxes imposed on their purchases of certain services while in Canada. However, the question of acceptable border tax adjustment on trade in services would seem to be one of considerable complexity.

H. Monopolies

23. Monopolies, including of the *de facto* private sort, would seem to be considerably more prevalent in the services sector that in the goods sector. Article VII of GATS imposes disciplines with respect to the treatment of "Monopolies and Exclusive Service Providers", its main thrust being that parties to GATS should ensure that such entities should not supply a monopoly service in a manner inconsistent with that party's obligations under the Agreement. There would seem to be a need for further study of the extent to which such monopolies could compete unfairly in the international market, as well as the extent to which they could "cross-subsidize" to provide services at less than cost with respect to their export activities.

[22/] With respect to the U.S. consulting services market, the Commission of the European Communities has claimed: "Federal contracts for consulting services (e.g. USIDA and the DOD) require US citizenship or 51 per cent ownership. Certified US permanent residency is not sufficient for a consultant to compete for Federal contracts." (See Commission of the European Communities, *op. cit.*, p. 40.)

[23/] Rules of origin within customs unions may create barriers against the provision of services such as engineering and design services. While some of the origin rules in the NAFTA currently preclude including in the value of net qualifying cost services related to marketing and sales promotion (including advertising), the growing importance of services in the economic industrial mix could lead to pressures for extension of the rules in this direction. Under the Canada/United States Free Trade Agreement, in the rules of origin for the automotive sector, the direct cost of processing is deemed to include design and engineering costs, thus encouraging this work to be carried out in Canada or the United States. (See discussion in USITC Publication 2460, *Rules of Origin Issues related to NAFTA and the North American Automotive Industry* (November 1991) p. 32.)

[24/] This has been described as the "partial destination principle". See G. Hufbauer and J.S. Erb, *Subsidies in International Trade* (London: MIT Press, 1984).

Chapter III

THE IMPACT OF SUBSIDIES ON SERVICE TRADE AND PRODUCTION

24. The DFA Agreement on Subsidies and Countervailing Measures provides guidance as to how to assess whether a subsidy has resulted in "serious prejudice". The criteria used are basically market shares in domestic, third-country or world markets and the comparison of prices with those of non-subsidized products. If such comparison is not possible, the existence of price undercutting may be demonstrated on the basis of export unit values. These criteria are reflected in national countervailing duty laws.

25. It is clear that for many services it would be difficult to obtain adequate data with respect to market shares and prices, and that the concept of "unit of output", and consequently, "unit costs" or "unit prices", might be somewhat inapplicable to many service sectors. Other problems would arise from difficulties in identifying the "origin" of services and from confusion between foreign and domestic firms (i.e., firms may be considered foreign under the GATS, but as "domestic" under relevant national legislation),[25/] as well as to what countervailing mechanism could effectively be applied in practice (as in most cases frontier measures could not be applied). For these and other reasons, authors who have addressed this issue have tended to argue against the establishment of a countervailing duty system for trade in services, on the basis that the data and conceptual difficulties would leave open the possibility of even greater abuse of countervailing duties than has been witnessed with respect to trade in goods. As far back as 1983, this question was addressed in a study conducted by the Office of the United States Trade Representative, which observed that:

> dumping and subsidy practices can apply to services as well as goods. However, careful consideration must be given to the technical problems associated with the computation of a dumping margin for service imports. The ability to legally measure sales at less than fair value is dependant, among other factors, on the ability to establish the value of the imported merchandise as stated in customs invoices. The complicated adjustment process involved in comparing home market to foreign prices could raise insurmountable technical difficulties because of the absence of specific documents in many service sectors. Enforcement of anti-dumping and countervailing duties could be difficult in cases where sales at less than fair value were found. Some services do not pass through customs when they enter the country making it impossible for customs officials to enforce the anti-dumping duties as is done in the case of goods.[26/]

26. This issue was addressed by the OECD Secretariat at the beginning of the Uruguay Round. It determined that:

> work so far has not yet enabled the scale of the problem to be accurately gauged, though it would seem to arise in some sectors. While on the face of it desirable, it would probably not be practical in most sectors to seek to transpose to services solutions derived from countervailing or anti-dumping duties. Should a country suffer injury as a result of predatory or unfair practices,

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[25/] For example, foreign-owned enterprises could still have the right to seek countervailing measure protection from the host-country government and could be covered by that country's competition laws.

[26/] Office of the United States Trade Representative, *U.S. National Study on Trading Services*, December 1983, pp. 91-92.

> provision might be made for it to be able to resort to more flexible offsetting measures. This aspect ... calls for further study.[27/]

27. Nevertheless some countries are beginning to arm themselves with mechanisms for dealing with unfair trade practices, (i.e., subsidies and dumping) which are perceived to be prevalent in certain service sectors. An important example was set by the European Community in the measure it formulated in 1986 in regard to "unfair pricing practices" in maritime transport. This measure was directed against the practices of certain shipping companies to set low prices to secure freight contracts. The practices deemed to be unfair were described as

> the continuous charging on a particular shipping route to or from or within the Community of freight rates for selected or all commodities which are lower than the normal freight rates charged during a period of at least six months, when such lower freight rates are made possible by the fact the shipowner concerned enjoys non-commercial advantages which are granted by a State which is not a member of the Community.[28/]

The United States regulatory regime on shipping also provides protection against certain "unfair" practices in the "rate standard for controlled carriers", and "predatory pricing provisions" of the 1984 Shipping Act.

28. Some countries have drawn up general trade legislation to deal with problems arising in trade in services on the same basis as trade in goods. For example, the Canadian International Trade Tribunal is empowered to:

> enquire into and report to the Governor-in-Council on any matter in relation to the economic, trade or commercial interests of Canada with respect to any goods or services or any class thereof ...[29/]

29. Many countries tend to avoid the use of countervailing duties although they have countervailing duty laws on the books, preferring to deal with all problems of price discrimination through anti-dumping actions. The imposition of countervailing duties to offset government subsidy programmes may continue to be a politically sensitive issue, as an attack on government programmes is invariably considered as more likely to provoke a more vigorous reaction than allegations of dumping against private firms. It would be difficult to envisage a system where action could be taken against subsidized imports but not against dumped ones, or to provide for substantially different mechanisms for dealing with injurious dumped and subsidized imports. As noted above, certain practices prevalent in sectors such as construction and engineering and media services could well be considered as dumping or subsidization, but a number of anti-competitive practices have been identified as having an important impact on trade in certain services, but which are not based on price discrimination and have been dealt with through competition law rather than frontier measures. The regulations drawn up by the European Community and the United States, as well

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[27/] OECD Trade Committee/Trade in Services, *Draft Report of the Committee to the Council TC(86)2 (1st Revision)* 6 March 1986.

[28/] Council Regulation (EEC) no. 4057/86, *Official Journal of the European Communities*, No. L378/14 31/12/1986, See also Jean-François Bellis, Edwin Vermulst and Philippe Musquare, "The New EEC Regulation on Unfair Pricing Practices in Maritime Transport; A Forerunner of the Extension of Unfair Trade Concepts to Services?" *Journal of World Trade*, No. 22, February 1988.

[29/] *Canadian International Trade Tribunal Act*, Section 18.

as by the International Civil Aviation Organization (ICAO), to discipline certain practices relating to Computerized Reservation Systems are a case in point.[30/]

30. At an earlier stage of the Uruguay Round negotiations, the question of price discrimination arising from subsidization was discussed rather inconclusively. Difficulties in, if not the impossibility of, calculating the price differential arising from a subsidy, and of the consequent injury to domestic producers have led to proposals that subsidies to services trade along with dumping should be dealt with under dispute settlement procedures or through competition law, rather than unilaterally.

31. Given the heterogeneity of service sectors, including the differences in the way that trade takes place as between sectors, the subsidy question might best be addressed on a sector-specific basis, as it would be extremely difficult to adopt a common approach to identify the trade impact of subsidies.

Chapter IV

PRIORITIES FOR FURTHER WORK

32. It is clear from the above that much pioneering work is required to (a) identify subsidies on services, and (b) assess their trade impact. The DFA provides that all parties shall exchange information concerning all subsidies related to trade in services that they confer upon or make available to domestic services providers. However, in implementing this, the following elements may need to be taken into account:

- there may be differing interpretations of what constitutes a subsidy among participants;
- adequate cognizance needs to be taken of the fact that the concept of trade in services extends beyond that of trade in goods to cover commercial presence and movement of natural persons;
- a proper compilation will require analysis of all government programmes (many of which will not be directly trade-related);
- it is possible that programmes related to trade in goods may also have an impact on trade in services;
- the actual practices in the case of subsidies may differ from the announced policies, depending on interpretation; and
- compilation of such information could be very time-consuming, particularly for countries with limited resources.

33. However, past experience in the GATT indicates that self-notification procedures on subsidies have been largely unsatisfactory in that governments have been reluctant to officially designate their practices as subsidies, as these might provoke charges of countervailing duty, and be used against them, in such cases. However, since - as has been discussed - the subsidies on services can constitute subsidies on goods exports, the possible criteria for countervailing action on subsidized exports of services have not been defined, and there may be a comparable reluctance to notify possible subsidies on services. Furthermore, the notifications on subsidies have been received from a minority of GATT contracting parties. Countries can be expected to have considerable difficulty in providing information on subsidies to services.

34. A more systematic identification of subsidies to services production and trade is a prerequisite to accomplishing the mandate of the Standing Committee to study the impact of subsidies on trade in services, especially on exports from

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[30/] See P. Brusick, M. Gibbs and M. Mashayekhi, "Anti-Competitive Practices in the Services Sector" in *Uruguay Round: Further Papers on Selected Issues* (UNCTAD/ITP/42). See also François Vellas, "Approche du secteur de tourisme international" (mimeo), UNCTAD, Geneva, May 1993.

developing countries. It would appear that in order to assist the Standing Committee in implementing item 3 (d) of its Work Programme, additional work may need to be undertaken by the secretariat. Such research could be carried out in collaboration with members of the Committee. This could involve a review of available material, including:

- official journals and gazettes;
- budget documents;
- trade action report by administrative agencies;
- reports on procurement and grants for research and development;
- reports of foreign aid and development agencies; and
- rules of origin in regional trading agreements and other relevant materials.

35. To ensure that this work will remain manageable, particularly in proceeding from the stage of identifying subsidy measures to that of attempting to assess their impact, it might be desirable to focus work on a sectoral basis from the beginning. For example, case studies could be conducted in areas where it is perceived that subsidies have a major impact on trade in sectors of export interest to developing countries (e.g., construction and engineering design services) National experiences in the use of subsidies to develop export capacities in service sectors could also be examined. It might also be useful to look at specific issues peculiar to trade in services such as those arising from the different modes of delivery. Such studies could examine possible benefits received by corporations to allow them to compete more effectively in world trade in services, including through commercial presence in foreign markets. The Standing Committee could provide guidance as to the appropriate direction of further work under the agenda item. Other international organizations could contribute to this exercise, and members could bring relevant studies or other data on this issue to the attention of the Standing Committee and the secretariat.